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By email: taxtreaties@oecd.org

Dear Ms de Ruiter

BEPS Action 6: Prevent Treaty Abuse (Revised discussion draft released on 22 May 2015 (the "Draft"))

We are writing to you further to our letters of 30 October 2014 and 7 January 2015 in relation to our concerns that the previous proposals in relation to Action 6 could deny Treaty benefits to debt funds (which, as in our earlier letters, we use in this letter to refer to debt funds, CLOs, securitisations and other special purpose entities established to advance or acquire loans to individual or corporate borrowers).

We are disappointed that our comments have not been taken into account in the Draft and we consider that those concerns remain relevant to the revised proposals in the Draft.

In our letter of 30 October 2014 we set out the reasons why we consider that Treaty benefits should be available to debt funds. Those reasons form the background to the comments on the Draft which are set out below, but, to maintain brevity, we do not repeat them here.

Our comments on the proposals in the Draft focus only on the treatment of debt funds. In short:

1. **General comments on LOB Rules** – We consider that, if the LOB Rule is implemented (in either the proposed simplified or full form), then it seems almost inevitable that many debt funds will be denied access to Treaty benefits.

   In the case of, in particular, securitisations and other capital markets entities, we consider that this result would be directly contrary to the general consensus which has built up over the last few years that revitalising the securitisation market and creating greater ease of access to capital markets is critical to widening the sources of funding available to businesses, and to filling the "funding gap" that has resulted from bank deleveraging (particularly for SME financing). [1]

[1] See for example, European Commission Consultation Paper: "An EU framework for Simple, Transparent and Standardised Securitisation" (2015); Bank of England and European Central Bank Discussion Paper: "An EU Framework for Simple, Transparent and Standardised Securitisation" (2014); Gert Wehinger, "Bank Deleveraging, the Move from Bank to Market-Based Financing and SME Financing", OECD Journal: Financial Market Trends 2012/1; OECD Round Table: "Non-Bank Debt Financing for SMEs: The Role of Securitisation, Private Placements and Bonds" (2014); European Commission Green Paper: "Building a Capital Markets Union" (2015).

Specifically, for debt funds issuing cleared notes (e.g. as part of a securitisation), it is simply not possible to identify the ultimate noteholders, as required by both the proposed simplified and full LOB Rule. Fundamental legal, regulatory and commercial changes to the way in which clearing operates in Europe would be needed in order to put issuers of cleared notes in a position where they could identify the holders of notes which they issued.

Identification is also difficult (albeit not in principle impossible) for debt funds that do not issue cleared notes, particularly given the fact that some debt fund investors are themselves funds or other intermediaries.

We note that FATCA and CRS were designed to avoid the necessity of tracing beneficial ownership to the ultimate beneficiary; disclosure and/or withholding takes place at the level of the last intermediary in the chain of payment/settlement and not (as Action 6 requires) at the level of the underlying borrower/issuer. This kind of "withholding agent" approach seems to us more practicable, fairer and less distortive than the LOB (given that it means all beneficial owners entitled to treaty relief would obtain it, and all beneficial owners not so entitled would not). However we appreciate that at this juncture so radical a change is unlikely to be considered by the Working Party.

We would, therefore, be most grateful if the Working Party could consider the question of how the LOB can be applied in practice, particularly in the context of cleared notes. Our preference would be for appropriate exemptions to be included in the LOB and simplified LOB; or alternatively for implementation to be delayed until practical details are resolved. However if the Working Party does not wish to do this, it would be helpful if the OECD could engage with a full range of stakeholders before finalising its proposals, given the implications for securitisations and capital markets.

(Alternatively it may of course be the case that the LOB will be adopted by so few OECD Members that it is of little practical relevance. However it seems to us that we (and the wider market) will have little visibility on the level of LOB adoption until it is too late to adapt systems and processes to deal with it.)

2. **Simplified LOB Rule** – As drafted, this would not assist debt funds. In most cases, they would simply not be eligible for Treaty relief.

   Debt funds are unlikely to be "qualifying persons" themselves, and, as they cannot usually identify their owners, they will generally be unable to determine if they are entities in which the requisite beneficial ownership is held by qualifying persons or by equivalent beneficiaries. Indeed, as noted above, for debt funds issuing cleared notes (e.g. as part of a securitisation), it is simply not possible to identify the ultimate noteholders.

   In most cases, debt funds will also be unable to meet the "active business" test. Unless Contracting States agree to extend the proposed excluded entities list, most debts funds are likely to fall within the "investment" carve out wording included in paragraph 4(a).

Accordingly, in order to benefit from Treaty relief, the *only* option available to many debt funds would be to obtain specific clearance. We are concerned that, without clear guidance on the circumstances in which clearance would be granted, there will be both uncertainty and a real risk that debt funds would not be treated in a consistent manner. As a result, reliance on the availability of discretionary relief would be commercially unacceptable to potential investors. Even if clearance could be obtained, there would often be delays before relief was granted. Unless the period of delay was reasonably certain in advance (and short), this is also likely to be commercially unacceptable to potential investors.

The effect would be to inhibit the access of residents of Contracting States (or at least those Contracting States that did not agree specific wording to cater for debt funds) to an increasingly important source of financing. This would put such entities at a significant disadvantage.

We therefore ask that, as a minimum, the Working Party consider:

(a) including guidance in the Commentary which makes it clear that in the case of debt funds, there is a presumption that clearance should be granted, which would be rebutted if the PPT is failed;

(b) following on from this (and to fully reflect EU principles of freedom of movement and establishment), amending any guidance along the lines of that set out in paragraph 32 of the Draft accordingly, and in particular, so that that wording relating to the position of entities with parents in third States is revised to deal with the position of investors in debt funds (and to reflect our proposal at (a)); and

(c) including guidance making it clear that requests for Treaty relief must be processed promptly (as reflected in the proposed guidance at paragraph 32 of the Draft), and in any event within the timetable outlined in that guidance.

It would also be helpful if specific guidance (including examples) relating to the application of the PPT to debt funds could be included in the Commentary.

3. **Full LOB Rule** – In our view it is helpful that the Working Party has concluded that it should continue to look at solutions to issues relating to the treaty entitlement of non-CIV funds.

   We note the concerns raised at, in particular, paragraph 24 of the Draft. Our view is that those concerns are not really relevant to debt funds – in relation to which, broadly, the commercial aim is simply to make available debt funding to borrowers on a tax-neutral basis.

   We consider it helpful that options to be discussed include adding a specific provision on non-CIV funds in the LOB Rule, and adding examples on non-CIV funds to the Commentary to the PPT rules, and we would urge the Working Party to proceed with both of these alternatives. We consider that, in relation to the second option (examples in Commentary) our comments at paragraph 2 are again relevant.

4. **Special Tax Regime** - Because of the importance of debt funds such as securitisations as a means of raising finance, a number of jurisdictions (such as the UK, Ireland, Luxembourg) have introduced special tax rules for securitisations. Broadly, those rules ensure that the SPVs used in such financings are subject to simplified tax rules, and bear no, or a nominal amount of tax. This means that the underlying corporate borrower is able to raise debt financing on a cost-effective basis (although in the great majority of cases this is a simplification rather than an absolute tax-saving, and typically regimes of this kind have anti-avoidance rules to prevent them being used abusively).

   As this proposal is drafted, SPVs falling to be taxed within the above special rules would be caught. Other debt funds that are taxed under rules (or practice) which provide for a preferential effective rate of tax would also be caught.

   Our view is that these onerous provisions are not necessary, and that, as drafted, they are disproportionate. Where it is appropriate to deny relief to entities falling within a specific tax regime, we think that this can be achieved through the application of the PPT.

   If, however, the decision is made to proceed with this proposal, then we would strongly recommend that consideration is given to extending the exception included at sub-para (vii) of the proposed "special tax regime" definition so that it extends to securitisation companies (and other debt funds). We see no reason why investment vehicles for real estate and securities portfolios should benefit from a specific exclusion to the proposed rules, but that debt funds should not. Indeed those debt funds that issue debt securities are in principle incapable of facilitating base erosion (i.e. because most jurisdictions will tax an investor holding debt securities in a very similar manner to that if the investor had held the fund's underlying debt assets directly).

   In addition, we would ask that relevant guidance (with examples) is added to the Commentary.

Please do not hesitate to contact us if you require further information in relation to any of the above.

Yours sincerely

Clare Dawson
Chief Executive

cc HM Treasury